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SUBJECT: Audio Recording of the bi-weekly Catalyst Funds open house conference call 10/25/16

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AUDIO TRANSCRIPTION

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P R O C E E D I N G S

MR. MINNICK: Welcome, everyone, and thank you for attending our bi-weekly Catalyst Funds portfolio manager's open house conference call.

Before we begin, I would like to remind everyone today's call may include forward looking statements. These statements represent the firm's belief regarding future events that, by their nature, are uncertain and outside of the firm's control. The firm's actual results and financial condition may differ, sometimes materially, from what is indicated in those forward-looking statements.

Please take a moment to review the fund's fact sheet and perspectives. These documents include some important risk considerations that investors should carefully consider, such as investment objectives, risks, charges, and expenses that can all be reviewed prior to investing in any of the catalyst funds. This and other information about the funds can be obtained by contacting our internal sales desk at 646-827-2761, on our website, catalystmutualfunds.com, or by reaching out to your regional representative.

Today, we have Ed Walczak and Kimberly Rios on the line who are the manager and co-manager of the Catalyst Hedge Futures, ticker symbol HFXAX and Catalyst

Hedge Commodities, ticker symbol H -- CFHAX funds.

Ed Walczak is a senior portfolio manager at Catalyst Funds and is responsible for the day-to-day management of the Hedge Futures and Hedge Commodities Funds. Additionally, Ed had been the portfolio manager of the Hedge Futures Predecessor Fund, Harbor Assets, since its inception in 2005 until its conversion to a '40 Act mutual fund in September of 2013. Mr. Walczak has a bachelor's degree in physics and economics from Middlebury College and a master's in business administration from Harvard University's graduate school of business.

Kimberly Rios is a portfolio manager on the funds and received her bachelor's degree in finance and economics from the University of Arizona in 1994 and received her CFA designation in 2001. Additionally, Kimberly has received her chartered market technician's designation in 2014 through the market technician's association.

As a reminder, all lines will be on mute during the overview of the call. If you have any questions, please hit star and then five at any time to place yourself into the queue. When we get to the Q and A portion of the call, I will announce you by your area code and prefix of your phone number, and you will hear

your line being unmuted.

With that said, folks, I will now hand the call over to Ed and Kimberly.

MR. WALCZAK: Thanks, Ed. Good morning, good afternoon, everyone, and thanks again for your participation on the call, your interest, and support of the funds. Let me start off with an update of the SMP fund, and it's a little bit -- it -- it will probably be a little bit repetitive for those of you that have been on the last two or three or four calls.

We've been in some pretty flat, low volatility market conditions over that period of time. One of the themes I've talked about in the last couple updates was that of trying to harvest some of our unrealized gains as we move through the different expiration cycles in the portfolio and how the principle risk to the fund's NAV was a sudden decline in the market before we were able to take those -- those gains off the table.

So, the good news is we're -- we're completing, or we completed in October as of last Friday the last expiration period in which we had substantial, concentrated, unrealized gains and we were able to take most of those off at pretty favorable prices. So, I've talked to you in the past couple of calls about some numbers and again, these are all approximate numbers,

and -- and relistened to Ed's risk or disclosure statement or caveats about forward looking statements, but I will tell you we're -- we're talking now more in the neighborhood of three cents NAV is probably a -- a good number.

So, we've -- we've removed that -- that risk of unrealized gains evaporating. We're now in a more normal scenario and -- and more importantly, one of the -- the large risks of the previous concentration of unrealized gains was that -- that those gains were concentrated in nearby expiration months, which means you've got options with one or two or three or four weeks to go and long option premium, and in that scenario, a market decline wipes out those options and -- and there's not much time left for them to recover, even if the market recovers.

So -- so, the good news to all of that is all of that situation has passed us now, and we do have a -- two or three cents unrealized gain in the fund now, but that's a normal condition, and it's actually spread across positions in November which have a month to go, and on into December, end of December, we have positions on in January, February. We just started to put February on and just started trading this week. End of January.

So, we've got some gains in some very small gains across all of those positions, and the good news is

even in the event of a sudden market decline, if -- if everything vanished, it would be a couple of pennies, and it's not likely that everything will vanish because we're spread out as we are more normally positioned. We -- we're back to a -- a normal positioning in that regard in that we're spread with -- with very small gains in many different expiration months, and now dependent on what the market does, whether those small gains turn into larger ones or whether we try to scalp a little bit more as -- as time passes.

With that, I wanted to give you a little more sense, too, where -- where -- in terms of how fully invested we are and -- and what we're doing in these current market conditions. I mentioned in the last call, I think I used the term that someone had a follow-on question about about being in no man's land, and unfortunately, we're still there, and what that means is we basically have no put positions on below the market. Those are our volatility positions.

We try to take advantage of volatility expansion, but we only do that when the -- the term structure of volatility flattens, and as you recall, if you are not someone that looks at or has the modeling or analytics to look at the term structure of volatility, that's the level of volatility built into options with

different expirations. It's different at 30, 60, 90, et cetera, but the shorthand. There's -- there's two short hands.

If you do -- if you look at the VIX, that's pretty easy to see on -- in the financial press or on a quote system, and you look at something called the VXV which is a 90-day number, if you compare those two when they start to get, say, within five percent of one another, then -- then you can rest assured that the curve is likely flattening. If you even don't want to go that deep, just look at the VIX.

It's got to approach 20 before you -- you get a -- a real flattening in that curve. I mean, usually, maybe 18 does it. Maybe 19 does it, but that's the -- the type of scenario where I could just look at the VIX and it starts to get up to those levels. That's still not necessarily high, but -- but it -- it's probably at a point where the curve is flat enough for us to start to put on put strategies. So, the -- the bottom line to all that explanation is none of that stuff has happened to any degree over the last, really, six months, so as a result, we have basically no put positions below the market.

At the same time, if -- if you both either recall or simply look at a chart, the last month or two

in the SMP has been kind of this -- this kind of flat, choppy, slightly downward movement, and what that's done unfortunately for us is it's -- it's -- the market has started to drift away from some of the places we put our profit ranges, so -- so, we're not in that sweet spot that we were in last quarter and led to some nice returns.

We're back into what I would call more of a scalping mode, meaning we put on positions, the market really doesn't go anywhere, some of the short sides of our positions decay a little faster than the long sides, so we're able to take them off at a small profit, but nowhere near the potential that we would have if the market were -- were in some sort of uptrend. The other issue for us in our strategy. So -- so, right now, volatility conditions say calls, not puts, but at the same time, the market action is not conducive to being very aggressive on the call side, either, and let me explain a little bit about what that means.

Those of you have -- who have listened to descriptions as a strategy will recall that we -- one of the edges we feel like we bring to the table with our strategy is that we don't take downside risk. We -- we take upside risk, while at the same time looking for upside opportunity and that means we put on call spreads

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that have a profit range. You've -- you've certainly heard me talk about profit ranges, and our risk is not to the downside because if the market tanks, then everything expires and we break even, but if the market goes too high too far, then that's where our risk lies and that's how we've chosen it.

So, how do we manage that? I -- I've talked about how volatility points us in either calls or puts. Further analysis of volatility tells us, "Hey, should we be doing January options? February options? December options?" So, once we are -- are driven by our volatility analytics to a -- a particular expiration month and as I mentioned, right now, February just started trading, we -- we would have traded February over the past couple of weeks based on volatility, but it's one of those real world constraints. February's series options began trading on Monday, and there's not much we can do about that.

So, we started trading options, February options. However, the next calculation we have to do is, as I mentioned, we -- we put on these spreads at different strikes, some long, some short, and it creates a profit range, and recognizing that our risk is to the upside, we are very careful to be conservative and not to place these spreads too close to the market.

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Well, what's too close? We're not in the business of predicting direction, but we do use some technical analysis and some fundamental analysis to take a real broad swipe at where the market might be out in February so that we can put a profit range in a place that gives us some opportunity, but more importantly, not so concerned about opportunity. We're really concerned first and foremost about risk. Our risk is to the upside. That translates into taking a swipe at where the market's going to be and ensuring that we don't place option spreads in a place where it would be easy to get run over, so to speak, by the market to the upside.

So unfortunately, when we put all this together, we said, "Let's trade February options based on volatility. Where do we want to be with February strikes?" And when we look at the combination of those two things, we're not finding tremendous opportunity and -- and what that means is the place that we would have to put positions on in terms of market levels, market strike prices for these options in order to meet the other criteria as a part of our strategy, how far apart longs and shorts are, what sort of -- you know, we want to go in and -- and do these at least at even money so that we're not exposed to time decay, all these other constraints that we use, when it all comes together,

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we're not seeing -- we're not seeing highly favorable trades.

So, what does that mean? We -- we're not in the business of -- of doing either one of two things. We're not in the business of taking trades that don't fit at all, so we don't do that. We're also not in the business of sitting on our hands entirely unless we really, really, really don't see anything at all, and where that leaves us is kind of at idle speed, and -- and that means as we are putting on February trades.

However, because these trades are at the higher risk end of our spectrum, meaning they're a little closer to the market than is optimal but still within our parameters, so our answer to doing that is we're just not putting on -- them on aggressively and -- and what the -- so, then what that means is we will be trading less on a given day, putting on less positions. We're -- we're far away from our position limits, and we're waiting for better opportunities to become more aggressive.

So, we're not sitting on our hands. At the same time, we're sitting here in a position -- October rolled off on Friday and that left us roughly 25 to 26 percent invested. Once again, recall that we don't invest our entire capital. We have position limits, number of positions per unit of capital, and on that

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basis, we're at about 26 percent. So -- so, fairly low.

We like to be above 50. We like to be really in the -- the 70 to 80 percent neighborhood where we have a little power to drive, but not much. We would be there if the conditions were right. They're simply not. So, we're putting on higher risk positions in smaller quantities.

Should the market conditions change as -- change, we'll wrap up -- ramp up our -- the level of trading, the level of positions we put on, and -- and increase that sizing, but for now, we do have positions on in November expiration, December, end of year expiration, mid-January, end of January, and we just started to put on mid-February, but the numbers of positions on are relatively small because we're not seeing that combination of expiration period based on volatility and price based on technical and fundamental risk considerations to put them on.

So, that's kind of where we are. Bottom line is we've taken unrealized gains largely off the table. That's good news. We do have positions on. We do have opportunity -- somewhat muted opportunity, but we do have opportunity until year end. We're putting on positions conservatively because the market is in a no-man's land from a -- from a price and volatility standpoint, and

that leaves us in kind of a 25 percent, 26 percent invested position looking for more, but not -- not going to force undo risk into the portfolio.

Let me -- let me stop there and turn it over to Kimberly to talk a little bit about The -- The Commodity Fund.

MS. RIOS: Thank you very much, Ed. Our current year to date numbers for the Hedge Futures is 11.32 percent and Hedge Commodity is 12.08 percent. Hedge Commodity is at $77 million, and we've been asked to give a little bit more insight into the funds on each call, so we're going to try to do that with each call going forward. Ed's going to do a little bit more today, and I'll start with some items on The Commodity Fund.

So, the commodities that we trade, they have option expirations that typically fall within the last two weeks of each month. So, last week, the November corner options expire and tomorrow, November Gold options will expire. As option ones drop off, new months become available to trade. For example, two weeks ago, our furthest month out was February. However, we are now trading commodities in March.

Last week, we booked some smaller profits in corn, while some of the positions just expired. Corn volatility is in its lower winter segment and we are

building positions into the early spring months when higher volatility is typical. Our current corn position is only about five percent of the commodity section of the portfolio. However, we will be increasing our allocation as we see more opportunistic trades. The current positions would prefer corn volatility to increase, and the price risk is present below $3.05 and above $3.65.

Oil is approximately 40 percent of the commodities section at this time. The next expiration is in mid-November, and we would prefer if volatility decreased and prices rose. We find this to be oil's typical relationship. Price drops, volatility rises, and in slow rising of flat markets, volatility declines. Over the next two weeks, we would prefer if oil climbed gently but did not surpass $15 to $7 in price. The downside risk is below 46.

With this lower volatility, we were able to take off some risk below the market, as some of the options that we had were relatively cheap, and we were able to buy them back at a very inexpensive rate. As for gold, gold is the largest commodity allocation right now at approximately 55 percent. The November gold expires tomorrow. Currently, the price is about $12.73 and we would prefer to stay above $12.50 into tomorrow's close.

So, about 24 hours from now.

Over the next month, the fund would prefer a higher volatility and somewhat flat prices. Volatility does tend to rise in the latter -- later months of the year, and we are coming upon an election and a fed meeting. Right now, we have a risk above $13.10 and $12.50 for options that expire above a third to fourth week of November. Right now, gold has the heaviest weighting, and we anticipate the weighting to look much different after the gold option expiration on November 22nd.

As of today, we've recovered the NAV loss that was attributed to the gold decline the first week of October. Gold declined -- gold declined sharply in price, then levelled off. The price move was not matched by a higher volatility move. Price for the flat and options of prices came together. So, this is a good example of how price does not have to fully recover to get redone in the fund's NAV. In this case, we just needed time to pass.

And with that, Ed, would you like to add anything?

MR. WALCZAK: Yeah. Just -- just kind of a general 40,000-foot overview comparison of the two funds. I think we've talked about this a little bit before, but

I want to reemphasize. We're really not price driven. Prices certainly, certainly do affect what we do, but volatility is the primary trigger for everything we do in both funds.

The real difference is you hear me talk a lot about price ranges and the SMP above the market. It's because in the SMP, and -- and in equity markets, there's this really strong relationship between volatility and price movement directionally. Price goes up, volatility comes out of options. Price goes down, volatility comes in. So, we've -- we've oriented -- we've locked in, really, the SMP fund to take advantage of that unique equity market relationship.

So, one of the reasons that we talk about price above the market is because we're using low volatility or short volatility structures above the market that actually make money more based on price movement rather than -- than movement and volatility because above the market and equities, you don't get much. When equity markets are going up, volatility is low and goes lower, but it's -- you know, the VIX goes from -- from 14 to 13.

So, that's not a big move. You're not going to make money on volatility, but these structures will make money as -- as price grinds higher, but the primary reason we use them is because of that volatility

relationship to price and equities. Similarly, below the market in the SMP fund, we all know that the VIX goes through the roof when -- when the market comes down. We try to take advantage of that with -- with volatility structures. We don't care about price. So, it's -- it's kind of cut and dry and locked in. In the three commodity markets we -- we trade, there's -- there's not that locked in relationship.

Kimberly mentioned in oil, what we've observed over the last year, for example, is when -- when oil was historically -- hitting historical lows, this really -- people were kind of panicking. This was -- this was, like, a major deal. Oil was going to 10 bucks a barrel. "Companies are going to go out of business, the global economy is crashing, et cetera." Lots of panic.

Lots of volatility got built into options, and we've seen that relationship with oil that -- that says, "Hey, when oil's down, volatility goes up. When oil goes up, volatility goes down," but it's not always the case. It's more normally the case in all the commodities that when -- when price move is violent, then that volatility gets into options, and when it's not, the volatility comes out. It doesn't often matter what direction the commodities are going. It really matters what volatility we observe.

So, these -- these relationships are kind of short term. So, what happens in the commodity fund is we don't -- we aren't locked into low volatility above the market, high volatility below the market in any of those markets. We simply look at absolute volatility and -- and Kimberly's done a huge amount of research on historical volatility levels and some of these price relationships, even though they were short-term, and that's what we use.

So, once we put these things on, we're putting on -- when we look around and we say, "Wow, gold volatility is historically low," then we're using our low volatility structures in hopes that we get a volatility spike, and if we get a volatility spike, we'll make money. Meantime, if we do get some price movement, we might make some money, we might lose some money. We have to manage that risk, but primarily, we're looking for volatility.

So, I think it's instructive when -- when Kimberly mentioned that oil declined. This was -- this was an oops moment because oil declined rapidly. There was severe price volatility. We had low volatility positions on, meaning we were positioned to take advantage of an increase in volatility. What happened was you got price volatility and no options volatility.

That's not very common, but it happens.

Markets do what they want, and so, how -- how the fund -- so, the fund got hurt because we didn't make any money on the volatility that we were positioned for. Price pressured some of the price exposure. In our positions, we lost money, and so the -- the neat thing about options and what we do is that we just look for these things to come together.

So, now we're in a situation where we had price volatility and no options volatility. We want one or two things to happen. We either want price to come down or options to catch up with price volatility, and that's what happened as Kimberly described. What happened is big move in price, no moves in volatility, fund gets hurt a little bit. What happens is they come back together, price goes flat, goes dead for a couple of weeks. That matches up with what priced into options. Everything comes back to normal, and we recover the drawdowns.

So, that -- that's a -- you know, a little bit of a long, rambling explanation, but -- but it's a -- a little more depth and a little more color on -- on how we used volatility and how we're really not as price-dependent as we are volatility dependent in both funds. Just there isn't that lock -- lock step relationship in commodities as there is in equities. Different market,

different opportunities, different -- different risks, but same strategies.

And that's -- that's all I've got, if you want to open it up for questions.

MR. WALCZAK: All right. Excellent. Thank you so much, Ed and Kimberly, for that.

So, a reminder, folks. To ask a question, please press star, then five, and it will raise your hand, and I will unmute your line. It doesn't look like we have anything in the hopper just yet, so we'll give it a moment. Once again, star five, folks. Okay, and the first question that we have popping up, area code 630-748. It looks like that hand went down.

MALE SPEAKER: Yeah, I'm here. Can you hear me?

MR. WALCZAK: Yes. Yes. You're on.

MALE SPEAKER: Okay. Hey, Ed. I had a quick question for you. In the -- in the SMP fund, if your positions are relatively short and they're being opened and closed, you know, let's say over a 4 or 6 month period, how has the -- how has the mutual fund gone up 25 percent since inception with capital gain distributions only being 2 and a half percent of the NAV?

MR. WALCZAK: Yeah. So, the -- the phenomenon there, and I'm going to use the -- the absolutely -- I

mean, it's a -- it's a caveat, but it's absolutely true. I'm not a tax guy, I'm not an accountant, I'm not a distribution guy. However, I will tell you that, like all '40 Act funds, to avoid serious double taxation hits, the fund distributes all of its net gains any given fiscal year.

However, those -- in -- in the case of the SMP fund, there has been extremely rapid growth. So, that -- when you see at the end of the year, we may have made X dollars, but that X dollars is now distributed to a much, much, much larger dollar base of shareholders, and so it essentially dilutes the percentage value of the distribution relative to the -- the actual percentage gains that were realized if you got in when the fund was small, so to speak.

And so again, that's -- that's the qualitative explanation. You've got to talk to your local CPA to figure out the -- the exact details, but it's -- if the dollar is being distributed, there -- but by the time that a year has passed, the fund has gotten so much larger than on a percentage basis. Those dollars are a much smaller percentage than the actual increase in value of the -- of the fund.

MALE SPEAKER: Could you please tell me what the assets under management were when the fund started?

MR. WALCZAK: Started as a mutual fund, or --

MALE SPEAKER: Yeah --

MR. WALCZAK: -- or starting for --? Yeah, as a mutual fund, that we started around $7 million.

MALE SPEAKER: And one year ago, approximation?

MR. WALCZAK: I don't know that off the top of my head.

MS. RIOS: I can get that for you in just a second.

MALE SPEAKER: Okay. Well, that answered --

MS. RIOS: We had $2 billion in the --

MALE SPEAKER: -- the question. I --

MS. RIOS: -- in October.

MR. WALCZAK: So, the fund has --

MALE SPEAKER: Mm-hm --

MR. WALCZAK: -- about doubled in size in the last year.

MALE SPEAKER: Okay. Thank you very much.

MR. WALCZAK: You're welcome. The important -- I'll give one follow-on to that. The important thing to know is there -- because one of the things that we -- we have heard this question before, and there's been some concern about some sort of deferred gain that, you know, you get in now and all of the sudden, you get hit with a big taxable distribution on gains that you didn't receive

as a shareholder because you just got in.

There are no deferred gains. Again, in a '40 Act world, I do know enough about accounting and taxation to tell you that it's a terrible thing not to distribute your gains because there's some onerous tax rates on -- on '40 Act entities. So -- so, we certainly do, and I -- I'm pretty sure that all the '40 Act mutual funds distribute every -- every dime of net gain they have to avoid that tax penalty to -- to the entity, and hence, the shareholders.

So, there -- there is not a deferred gain sitting out there that if you buy the fund today, you're going to get what somebody else has gained from seven months ago. It's a scenario where, if the fund, for example, were to -- were to level off and not change its asset base, you should expect then, if the fund makes 10 percent in a year to get a -- a distribution somewhere much closer to 10 percent than we've seen over the last couple years.

MALE SPEAKER: Thank you.

MR. WALCZAK: Okay. Thank you for that. It doesn't look like we have anything popping up here. Once again, folks, star five to ask Ed or Kimberly a question. All right (inaudible). All right. So, first one. 605-271.

CASEY: Hi there. This is Casey. I'm in Sioux Falls, South Dakota. Just -- I'm just curious. So, we've -- we've actually invested into your guys' fund just starting this year, and obviously we've been happy with how much of a run that it's went on. And the thing that kind of baffles us is looking at the spread versus your competitors. It's so wide that we're curious -- is it just because that you have -- you're not playing the downside on the market that you're getting such different results? Or what do you guys attribute this wide of a spread against your competitors to?

MR. WALCZAK: So I have to ask which sort of class of funds or what kind of folks are you comparing us to in terms of competitors?

CASEY: I'd say -- I mean, so like, we're LPL people, so like even like -- one of their managed futures strategy is like an AQR, which I know it's different than a hedge future strategy like you guys are doing, but you look at that and there's almost a 13 percent year to date performance discrepancy. So I mean, I know that they're different strategies, but that is just -- that's a huge number when you're looking at something in the same class. And just curious what you guys really attribute to why you would be able to out-perform by that much.

MR. WALCZAK: Sure. Well, in general, we do

consider ourselves to be somewhat of a unique strategy. We're in the managed futures category primarily because we have -- we're an options strategy. We happen to use the S&P futures contract as an underlying, and that lands us in the managed futures category. However, most -- my understanding, at least, not staying completely up to speed with a lot of the other guys out there, but many in the managed futures space I believe are trend followers. Used to be I could say with some confidence there were trend followers in commodity markets.

Commodity markets have been difficult over the last five years or so, and as a result, last time I peeked under the hood on some of these guys is they -- they've sprinkled in some equity exposure because that was something they could ride. We've been in obviously a long-term equity up-trend, so that was something they could ride, so a lot of the managed futures guys kind of sprinkled equities into what used to be a commodity type of scenario. But all that being said, I'll get back to what we believe to be our edge overall, and that is we use a risk-limited instrument. Our edge lies in all about how we manage risk.

We're not looking for a way to make money, we're looking for a way to avoid losing money. And we're looking to earn return in a risk-limited fashion. And

again, we have some things that we're proud of in terms of strategies we've developed over the years. However, I will tell you there's no genius going on here. The genius is starting with an instrument called an option that has risk limitation built into it. You pay 10 bucks premium for your call option, you have most of the upside in the world, and you have $10 of downside even if the S&P is down 20 percent in the next month.

And I think that's an underappreciated quality from all the folks out who are spending enormous resource and analytical horsepower to try and decipher what's going to happen next, up or down, in whatever market they're in. I think that's tremendously difficult, so we don't do that. We use instruments that allow us to participate in, in some cases, directional moves with very, very limited or zero risk in the other direction. And I think if you can develop a strategy like we have to put yourself in that place, then you see the results, and that's what accounts for the alpha that we deliver. And I just think it's an under recognized phenomenon and it's an under recognized -- analyzed space in terms of the options markets and the particular kinds of strategies that we use. And in my mind at least, that's what accounts for some of the outperformance you're seeing.

CASEY: So just as a second part of my question

then, so understanding -- your guys' strategy actually changed then from not being -- like, from not actually playing the downside? Because 2008, your guys' fund absolutely knocked the cover off the ball, but if it was the same strategy that you're employing today, I don't see how you guys would be able to rack up those types of returns. So have you guys changed the perspectives investment objective or any big changes that, if this 2008 occurred again, that you guys would be able to catch that? Because it doesn't sound like it would be able to.

MR. WALCZAK: Yeah, actually our strategy's exactly the same, and I don't know if you've been on a call where we talk about how we made money in '08. We did not make money on downside price movement. The fund strategy does not predict price movement in general, although we do position ourselves to make money in equities to the upside because that's what they do most of the time, and that's where options volatility leads us to make money. So the downside, as I mentioned earlier in the call, we all know that when equity markets decline, volatility expands. So we are able to take advantage of the impact of expanded volatility and options pricing to make money to the downside. And that's actually -- in those markets is the place where we can hit a home run, because we can make money to the

upside the same as anybody else, pretty much dollar-for-dollar.

We limit our risk, but when markets go grind higher, we like to keep up with the S&P. This year, we've been fortunate that markets have behaved exactly how we would like them for the most part, so we're outperforming. But to the downside, we take advantage of volatility and volatility has an exponential impact on option pricing, not a linear one, and that means you can start having two and four and eight-fold moves and options for one-fold moves in price.

So to the downside, we don't care about price. We only play volatility, and if you recall in '08, we're all -- we all get excited when the VIX goes to 20, well the VIX was at 85. Now not only is that a four-fold move, remember that volatility acts exponentially, so now you're talking about 16 and 32 and 64 and 256-time moves when volatility starts getting that violent. And so it's almost inconceivable, I think, to a lot of people, people who have forgotten if they were around in '08 or weren't around in '08 of a VIX at 85. I mean, that's unbelievable.

But if the VIX is going to 85, what we do can have a huge benefit. We haven't seen a volatility expansion -- we may not see a volatility expansion like

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that in our lifetime, but even a normal -- last time we had a normal volatility expansion was in 2011. And we do the same things that we have done in 2008 and in 2011. 2011 was a good year for us. 2008 was a great year. Again, VIX at 80, can we make 50 percent when the VIX goes to 80? There's no reason we can't. Can we make 16 or 17 percent when the VIX is in the 30s and 40s for three of four months like 2011? Yeah we can still do that. We do the same things.

MR. MINNICK: All right, thank you for that. Looks like the next question that we have coming up is from a 248385.

PARTICIPANT: Hi, my question is regarding the distribution of the capital gains. Is there a certain date that you have pegged when you're going to actually distribute the (inaudible) capital gains?

MR. WALCZAK: I think there is and I think I don't know it. I don't know if, Ed, if you have any insight to that, but again, that's not the part of the world that I look at carefully.

MS. RIOS: I will chime in and just say the past two years have been around December 18th.

PARTICIPANT: Okay. Thank you.

MR. MINNICK: And we don't have a firm date yet on the internal (inaudible) side. Probably when we get

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our closer numbers mid-November, we should have the firm date that you're going to see those.

PARTICIPANT: Okay, thank you.

MR. MINNICK: Okay, and next question we have coming up, 479553.

PARTICIPANT: Hi, Ed. It's my understanding that as a goal you shoot for about a maximum draw-down of 8 percent. Specifically what happens to the fund if that were to occur?

MR. WALCZAK: So -- and you're correct, that is the goal of our risk management process and protocols. And let me describe a little bit about how that works. So we're not using a standard sort of stop-loss, although if we somehow get to 8 percent -- and we have been there actually in the fourth quarter of 2014 -- we will flatten that risk at that level. And there's always some slippage to be very honest.

When I instituted -- when I was the only guy involved -- instituted this risk, this particular set of risk rules that's been around. I did it in the middle of 2007. My actual thinking was if I set this thing up to control to 8 percent, if we get a -- just some sort of horrific illiquid, world is ending kind of market, we're probably, from a pure slippage standpoint, we're probably risking another maybe 200 basis points, another two, and

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I wanted to keep it to single digits. So 8 is designed to keep it under 10, but we've been successful in actually keeping it -- I think our worst draw-down, that 2014 draw-down, might have been about 8 and a half percent. And so we're happy, I'm happy with the performance of that system over time. But let me tell you a little bit of how we do it. In other words, we're not kind of sitting here waiting until we hit 8 percent, and then we jump up and liquidate the fund.

We consistently model the fund's portfolio. So there's a lot of different -- I talk all about term structure, about volatility and price ranges, and fundamental and technical guesses at where the market's going to go, and on and on. And what that does, it leads us into a pretty diverse collection of options positions in the portfolio. It's a little rare right now that we're only in calls, but so be it. But at any given moment, we have this portfolio that's got options all over the place. And so, although we entered each of these positions for different reasons at the time, we aggregate that into an overall portfolio, and in fact this is really one of the most important things we do, the entry is fairly mechanical, and where a lot of the brain power comes in is to manage the risk. I've said that before, I think that's our edge.

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So we aggregate all these options positions into a portfolio, and if you look at the portfolio, even those of you who are somewhat familiar with options and you can do kind of back of the envelope, expiration, here's what's going to happen kind of things, I guarantee you if you look at this portfolio, you have no chance of getting your head around it without some pretty decent options modeling software. So good news, we've got it, and what we do is we look at the portfolio and we actually graph the change in value of the portfolio over whatever price range we want to choose, and we generally choose a downside look of 15 percent and an upside look of 10 percent. And we will actually, when markets get volatile, which is you lead to the downside, we'll typically extend that downside look to 20 percent.

So imagine you're looking at a graph and the graph on the X axis has the value of the portfolio, and the graph on the Y axis is the price of the S&P, and so you can immediately see on a continuous basis what's happening to your portfolio value. And we can go in there with our -- with the tools in the software and peg a minus-8 percent, a minus-10, a minus-5, et cetera, and see those levels. We also, because options are time-based, we look across five different timeframes. We'll typically start at the furthest expiration, which right

now is out in February, and the software by default will divide, between now and February, into five chunks of time. So it will say -- I don't even know off the top of my head what that is. It's probably 120 days, so call it -- it'll give us 25-day intervals or something. So we'll see five lines on this graph at each timeframe and they'll be different.

So we then analyze this and say, "Where do we get in trouble?" and in trouble like -- as you correctly said, is -- trouble is down 8 percent. So we now look, where are we down 8 percent, and then we make -- we look where we're down 8 percent and look to see what does it take -- first of all, do we need to take action, is it -- and we have some rules around this -- are we down 8 percent if the market moves 1 percent next week? Well that would be a big problem. We would jump in right away and adjust the portfolio to whatever extent we had to take that off the table. In other words, the first thing we do is why are we down 8 percent. Oh, we're down 8 percent because the market is up. How do we protect against an up market? We buy call options. That's what call options do. If you're somehow being hurt by an upside market move, buy calls. In our case, we're short some calls out there, we'll probably buy them back. But -- so we look at all these parameters, and when

they're out of bounds according to our rules, then we identify why are they out of bounds. Maybe they're out of bounds because we're not hedged against a spike in volatility, for example. Maybe we look fine on price but we know that when price declines the VIX is going to pop. We go into our mode and we say what does this curve look like if we increase the VIX from 15 to 25, and at 15 we look fine, at 25 we don't look so good, we say, "Oops, we have a volatility exposure." How do you solve that? Well you can solve a volatility exposure a lot of different ways. One way is to simply buy a bunch of put options.

Normally we don't have to worry about that because we're always long puts -- whenever we have anything on down there. But an any rate, so this just gives you some qualitative sense for what we do. We're always looking forward. This is the only predictive thing we do. We react to markets to put on positions, but we try to predictively look at risk. We try to say if three weeks from now the market is up 10 percent, are we in trouble or not in trouble, and we've got definitions about what trouble means designed to keep us ultimately from an 8 percent loss. So we look at these things, we identify if we're in trouble, why are we in trouble? Is it price? Is it volatility? Does some time

have to pass? And then we take corrective action, and once again, we have a serious advantage, as I said, by simply using options because they're risk limited no matter what we're doing with them. The second thing to know about options is essentially options are hedging tools.

So the very thing we trade in that does sometimes give us risk is actually the same thing we have to go out and use to hedge when we discover we have too much risk. So we're -- the option -- we believe that the options contract's a beautiful thing. When we find a problem based on our portfolio model, we can almost always solve it. In fact, we spend a lot of time on figuring out how best to solve it.

We can use straight option purchases, we can use options spreads, we can use all sorts of combinations to give us just the right hedging exposure to bring that portfolio back in line where we take that 8 percent risk off the table. All that being said, there are times when we hedge, the market keeps coming, we hedge some more, the market keeps coming. When we hit that draw-down, we will go absolutely neutral. It doesn't always mean cash, but it typically means that -- a neutral exposure, where whatever the market does, we're not going any lower, and that's -- nothing in the business is guaranteed but

that's our goal, that's kind of how we approach it.

PARTICIPANT: Thank you.

MR. MINNICK: All right, excellent. Doesn't look like we have anything in the queue right now, so I'm going to go ahead and call last call on question, folks. Just press *5 and you can ask a question of Ed and Kimberly. Let me see, it looks like we've got a couple popping up here. We've got a 401793.

PARTICIPANT: Hey, Ed and Kimberly, could you comment on the correlation between the two funds and would you advise to combine the two to further diversify?

MR. WALCZAK: I -- I don't know, Kimberly, if you have any stats on this, but I would say just qualitatively that a couple things -- and we've said this before. One is, the S&P fund, because we run it as a neutral fund even though it's based on the S&P, it has a pretty low and a little bit negative correlation to the S&P. So I know that many out there use the S&P fund in their non-correlated asset bucket, and I think that's appropriate.

At the same time, the commodity fund -- Kimberly is wanting me to do sort of math in public by putting a chart in front of me and expecting me to understand it. Instead I'm going to let her look at it and explain in a minute, but the commodity fund, because

we're in completely non-correlated underlyings -- in other words, all right, here's the S&P fund, our market is the S&P, yet we're still very low correlation to the S&P. Commodity fund we're using the same non-directional options strategies and yet we're in completely non-correlated -- well, normally non-correlated markets. So we would expect that the commodity fund would be (A) not correlated to the S&P fund because of the different markets even though it's the same options strategy, and (B) even more reliably non-correlated to the S&P, again because it's a non-directional fund using non-correlated markets.

Here, I'll put a big asterisk next to that. There are times -- and I think many of you are aware of times -- most recent example is oil and to some extent gold has also exhibited some correlation -- both these markets have temporarily at least exhibited a correlation to the S&P. There was a time when investors in general -- a time meaning in the last six months, when oil was again setting historical lows -- when investors in general were so concerned about the impact of oil that oil inequities had a 90 plus correlation. In fact, I think if you run the numbers, the commodity fund has a largest than expected correlation to the S&P in the first year of its life, probably because one of its main

markets, oil, had an unusual -- now, it's done now. It doesn't work that way anymore, but had an unusually strong correlation to the S&P, and that will happen for short periods of time -- short periods of time meaning six months or so or even nine months or certainly less than a year. But generally speaking, we would not expect the funds would be correlated to one another, and especially the commodity fund to be reliably non-correlated to equity markets, and the asterisk to that is, I think we've all seen, that there are occasional pretty strong correlations, but short-term correlations between commodities and the overall equity market.

MS. RIOS: And I would just like to add to that. So for one year of inception of the commodity fund, we did a 12-year number on the Zephyrs (phonetic). So coming from Zephyr's, the hedge commodity has a (inaudible) 0.36. For that same time period for hedge futures was a negative 0.13. And as Ed was describing, in February, stocks went down as oil went down. Things became quite correlated at that time. We do have similar standard deviations, though. Hedge futures is about six and hedge commodities is just under eight. But we do expect to see a little bit different numbers the longer that we have -- the more months that we put on the board. So to say, just due to the February decline -- January-

February decline of oil and stocks being so closely correlated.

MR. MINNICK: All right, excellent. Looks like the next one that we have coming up, 509622.

PARTICIPANT: Yeah, I was just wanting to find out if you could give us an example of the volatility of -- an example of your volatility trade, just how the structure is.

MR. WALCZAK: Sure. What we do -- and this applies to both funds and all markets in which we want to capture an increase in volatility. But I use the S&P fund as an example, because again, we're locked in there to this relationship that says we're using volatility strategies underneath the market and more price-based, low-volatility strategies above the market.

But below the market -- and the reason the term structure of volatility is so important in these trades is that the normal term structure of volatility says that the VIX, which is a 30-day to expiration measure of how much volatility is assumed into option prices on the S&P 500 stocks -- so the VIX is a 30-day to expiration volatility number representing the nearby point in the curve if you look at it monthly, which is what we do for the most part. You then can look at a 60-day number and it's usually higher, and the 90-day is higher still, and

120-day is higher still, and at some point it flattens, but the curve goes from cheap to expensive in terms of how much of volatility is built into options pricing. So our strategy is to buy and sell different points on the curve. That means we're going to buy and sell in different expiration months, and we're going to be buying and selling not only different levels of volatility because the curve is different at different points, but more importantly different sensitivity to volatility. The longer -- it's actually fairly simple. The longer the time to expiration for an option, the more it is actually sensitive to volatility. So an option that expires 90 days from now will react more to a change in volatility than an option which expires in 30 days. So we want to sell the one that is less sensitive to volatility, meaning the nearer dated option, and buy the one that is longer dated.

And then if the market behaves, which it never does, but if it were to behave, meaning if volatility rose in lock step, if volatility rose the same on each point in that curve, then we'd be owning something that rose in value faster than something that we were short. Now, it doesn't happen that way because what happens in the real world is people panic, they look for insurance, they buy options -- put options, that's what jumps the

VIX. But people are cheap even when they're panicked, so they're buying short dated options because they're cheap, and they're bidding those prices up much faster than they're bidding the longer dated option pricing up. And what that means is when you see the VIX spike, that's great news that volatility is going up for our strategy. However, the option that we sold, the volatility built into that option is rising much faster than the one we bought, so that beautiful world where volatility rises the same and we're owning the one that it effects more isn't in place until that curve flattens. So once people get the initial panic out of the way, they've driven up the VIX, they haven't driven up the other options, that's when we step in and we now sell that nearby put option -- nearby by expiration -- we buy a longer-dated put option. We like to do that without spending any money because we've taken time decay off the table, and now we've bought and sold at parity.

So now the VIX went to 20 and that 90-day option volatility also is at 20. Now we know that from here, if the VIX goes to 40, that 90-day is probably going to follow fairly closely, and that's where we make our money because the 90-day option increase in volatility will be -- will have a bigger impact on its price than the nearby option that we sold. So it's

really -- I'll distill it down. If you open up Options 101, somewhere around about page seven, you're going to hear about a calendar spread and that's what it is. Now, we play around with where we put that calendar. Do we sell a 60-day option, buy a 120-day option, buy a 90-day option? Do we sell a 90, but a 150? That's the nuts and bolts of our analytics and our strategy and our secret sauce. And which strikes do we put them at? Do we sell one that's 100 points away from the one we bought? Do we sell it 200 points away? All of these things factor into exactly what this position looks like, but it's essentially a calendar trade where we're selling nearby, buying long-term. That gives us a long volatility exposure as long as we're careful not to enter this trade until we have parity or close to parity in volatility between the two options. And then from there we can make money if volatility continues to expand.

PARTICIPANT: Thank you.

MR. MINNICK: All right, next one we've got coming up, 858513.

PARTICIPANT: Hi, Ed and Kimberly. Larry Stucker (phonetic) in San Diego. Real quick, on the commodity fund, if you -- I know it's just fairly new. Have you done any of the work with regards to draw-downs similar to the hedged futures strategies fund?

MR. WALCZAK: Yeah, we have, and it's got an interesting wrinkle to it. We intend to deliver the same sort of 8 percent cap. The extra difficulty comes into the fact that we're dealing with three markets and not just one, so that you can have the perfect storm effect where -- you certainly can't go out and control to 8 percent of the fund in each of these markets, because you can clearly have an 8 percent draw-down in oil and a 2 percent draw-down in gold, and lo and behold you've got a 10 percent draw-down for the fund. So we do pay attention to modeling some of the perfect storm conditions, but it does introduce an additional level of uncertainty.

We think we have that -- we did have a very, very quick short draw-down earlier this year in the fund, and we think that taught us some lessons about how to control those events in the future. But we're modeling both allocation -- capital allocation and, really, risk allocation across these markets and perfect storm scenarios to make us control to the 8 percent.

But I will tell you with full transparency, it's a little bit less certain than what we're able to do in the S&P, both in terms of the fund's history and in terms of the triple markets. We have a good feeling about it now, but we are constantly looking for ways to

improve.

PARTICIPANT: Thank you.

MR. MINNICK: All right, excellent. At this time, it doesn't look like we have any more questions. We'll give it one more minutes. *5, folks, for any last minute questions for Ed and Kimberly. All right, so it doesn't look like anything's popping up here.

Well, Ed and Kimberly, thank you so much for joining us today. As a reminder, folks, the next call will take place November 15th at 2:00 p.m. which is changed from the traditional one o'clock EST slot that we usually go with. But thank you all for joining us. If you'd like, this will be available for replay, so reach out to your regional representatives and we can get that out to you. Have a great day.

Just clarifying, because you guys are aware of who NFR is and have had some interaction with them in the past. And I'm going to share something that I'm going to ask you to keep confidential, but I think it may be helpful as background.

We -- as you guys know we have a relationship with them and we pay them a trail on all our book of business where we use their activity. And the key relevant part here, though, which I think is important, is that the arrangement I have with them -- it is a deal

that we struck with them however many moons ago -- is that we have an in perpetuity exclusive license based upon maintaining some modest asset threshold.

The corresponding element of that is that -- and in fact the contract envisioned that over time we're going to develop our own capabilities -- is that we continue to pay NFR, if you will, a full fee on all assets that meet some certain definitions; but which all of our U.S. equity strategies -- which is really all they're being paid on now -- but the U.S., anything that sort of meets the standard definition of what we call the AlphaSector Premium, AlphaSector Rotation, they get paid on regardless whether or not it's our signals or not. And as I said, the contract specifically --

(End of recording.)

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CATALYST HEDGED FUTURES STRATEGY FUND.

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